

Version 4.1 August 2021

# **China CITIC Bank London Branch**

## **Risk Appetite Statement**



## Document History

<b>Owner</b>	Chief Risk Officer	<b>Status</b>	FINAL
<b>Version</b>	4.1	<b>Date</b>	8/2021
<b>Approved by</b>	Audit & Risk Committee		
<b>Approved Date</b>	16/8/2021	<b>Next Review Date</b>	03/2022
<b>Location</b>	London		

Version	Owner	Approval	Date	Change history
1.0	President	President	May 2018	PRA Regulatory Business Plan
1.1	CRO	MANCO	Oct 2018	Update to finalize PRA RBP – see RAS dd 24/10/2018
2.1	CRO	MANCO	Aug 2019	Updated – see RAS dd 6/08/2019 presented to ManCo
3.1	CRO	MANCO	Mar 2020	Updated – see RAS dd 22/05/2020 presented to ManCo
3.2	CRO	ARCo	Aug 2020	Updated – see RAS dd 17/08/2020 presented to ManCo
3.3	CRO	ARCo	Nov 2020	Updated – see RAS dd 26/11/2020 presented to ManCo
4.0	CRO	ARCo	Feb 2021	Updated – see RAS dd 22/02/2021 presented to ManCo
4.1	CRO	ARCo	Aug 2021	<p>The following has been added to the RAS:</p> <ul style="list-style-type: none"> <li>• Business activities – reviewed / updated (12)</li> <li>• Target Market – reviewed CITIC Group (13)</li> <li>• Target Market – reviewed HO FI (14)</li> <li>• Target Market – reviewed HO Corporate (14)</li> <li>• Target Market – deleted Local HO customer (15)</li> <li>• Target Market – reviewed EMEA/Other (16)</li> <li>• Customer/Product matrix – reviewed / updated (17)4</li> <li>• Credit Exposure – reviewed and updated (19)</li> <li>• Credit Definitions – updated (20)</li> <li>• Credit concentration – single entity changed to 12.5% (21)</li> <li>• Credit concentration – Group added 25% (22)</li> <li>• Credit concentration – removed low risk transactions (22)</li> <li>• Maturity profiles – reviewed and updated (23)</li> <li>• Credit mitigation – reviewed and updated (23)</li> <li>• Risk profile – reviewed and updated (25)</li> <li>• Sector/ Industry – reviewed/updated (25)</li> <li>• Customer/product matrix – updated (26)</li> <li>•</li> </ul>

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## 1 Background

This document sets out the Risk Appetite Statement (“RAS”) for China CITIC Bank London Branch (“CNCBLB” or “the Branch”). CNCBLB is the UK branch of China CITIC Bank (“The Bank” or “Head Office” or “HO”) and operates in London as a wholesale bank authorised by the Prudential Regulation Authority (“PRA”) and the Financial Conduct Authority (“FCA”), together known as ‘the UK Regulators’. In this document the Branch will identify, define and manage the key risks faced by the business it carries out. The RAS is a key component of the Branch’s overall Risk Management Framework (“RMF”) and allows the Bank to formally define its appetite for the risks it is exposed to.

The RAS considers the UK regulatory requirements, the delegated authority provided by the Bank (see **Appendix A** – HO Delegated Authority and **Appendix B** – Financial Markets Delegated Authority) and, where appropriate, the RAS of Head Office.

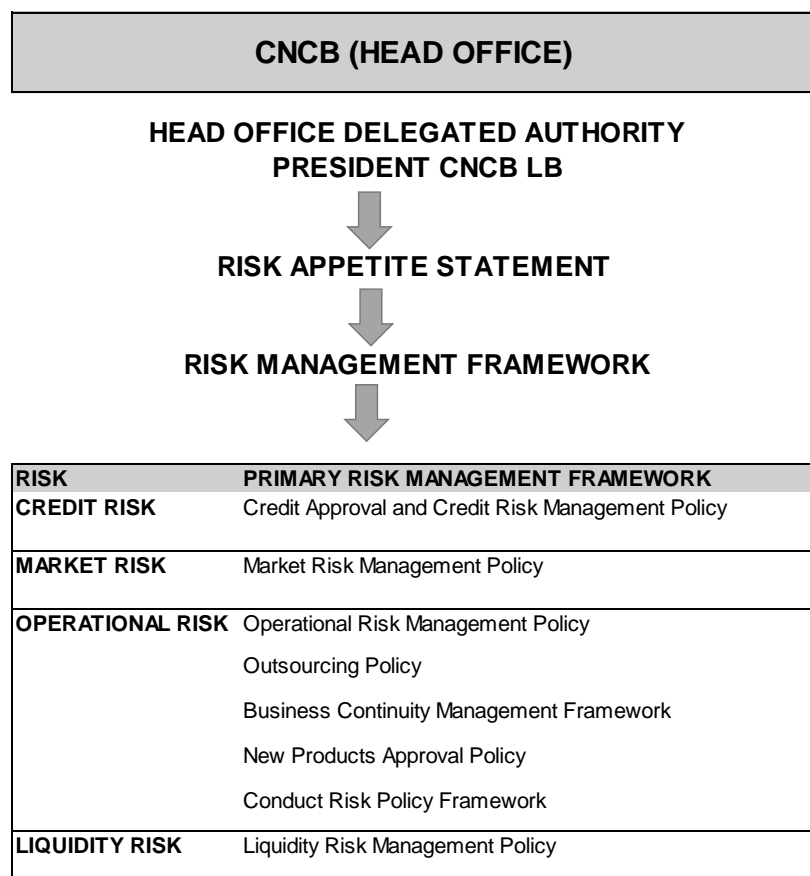
These risks include strategic and financial risks, largely as a result of the economic and political environments that the Branch operates in, and the credit exposure in respect of its lending and investment activities within the business and the treasury operations. The Branch accepts that these activities generate risk and will put in place appropriate systems and controls to manage the risks within the Risk Appetite and strategy established in the Business Plan. CNCBLB also recognises various operational, conduct and reputational risks which are managed by way of appropriate systems and controls proportionate to the size and complexity of the Branch which is supported by a strong risk and compliance culture implemented through a range of policies. Although the Branch accepts that it is neither possible nor desirable to negate all the risks associated with its business, the Bank is very cognisant of the importance of stating clearly, understanding and of managing these key risks appropriately within the approved Risk Appetite Statement.

## 2 Scope

This RAS sets out the approved business activities to be carried out by the Branch and the amounts and types of risk that the HO, through its delegation of authority (“DOA”) to the President of the Branch has authorised the Branch to undertake. It also documents the associated governance, oversight, monitoring and reporting framework.

## 3 Objectives

The RAS sets out the parameters that determine which business activities will be carried out by the Branch, and defines the types and levels of risks that the Branch is willing to accept in order to achieve its business objectives. The RAS forms an integral part of the Branch’s Risk Management Framework and should be read in conjunction with CNCBLB’s risk policies and overall risk framework:



The Branch defines ***Risk Appetite***, as the aggregate level of risk it is willing to assume within its 'Risk Capacity' in order to achieve its strategic objectives as expressed in its business plan.

***Risk Capacity*** for the Branch is defined as the maximum level of risk the CNCBLB can assume before breaching constraints determined by:

- i) the delegated authority granted by HO for the Branch to enter into transactions on its behalf; and
- ii) the regulatory regime it is subject to within the UK including, from a conduct risk perspective, its obligations to depositors, other customers and stakeholders.

The Branch's risk capacity is governed by a number of criteria:

- The DOA provided by HO to the President;
- The DOA provided by HO Financial Markets;
- The PRA and FCA Handbooks;
- Availability of working capital; and
- Access to liquidity (including through HO borrowing).

Risk limits have been set within this document that quantify as far as possible the risk appetite of specific risks the branch is willing to take, and this provides a framework within which the business must operate. The RAS risk limits will be monitored and reported to the relevant Committees and ManCo, at least monthly. As an 'Early Warning Trigger' any exposure reaching 80% of the limits must be highlighted to the CRO, relevant Committee members and ManCo.

The ManCo members will provide guidance on the action required and timeframe.

#### 4 Document Ownership

The 'ownership chain' of this policy is detailed below.

<b>Document Owner</b>	<p>The Branch's Chief Risk Officer ("CRO") is responsible for the maintenance for this RAS.</p> <p>The CRO will also be responsible for reviewing the ongoing adequacy of the RAS and will review it at least on an annual basis or more frequently as required. Any proposed changes to this document must be formally approved by the ManCo. Changes may also require notification to the UK Regulators.</p> <p>The CRO will recommend this action as appropriate for the ARCo to consider.</p>
<b>Oversight and challenge</b>	<p>The ARCo will review and challenge this document at least annually or more frequently as necessary. It will provide challenge to any changes suggested by the CRO</p>
<b>Approval</b>	<p>ARCo is ultimately responsible for the approval of this RAS and for ensuring it is set within the parameters of the President's and other Head Office DOA's.</p> <p>ManCo will have oversight and note ARCo's approval to ensure it is in line with the overall Branch strategy.</p>
<b>Applicability</b>	<p>All members of staff, whether permanent (local hires and/or expatriate) or contractors must operate in accordance with this document as disseminated through policies, procedures and risk limits as applicable to individual roles.</p> <p>Escalation of any matters arising in respect of this should be via the individual's Head of Department or directly to the CRO.</p>

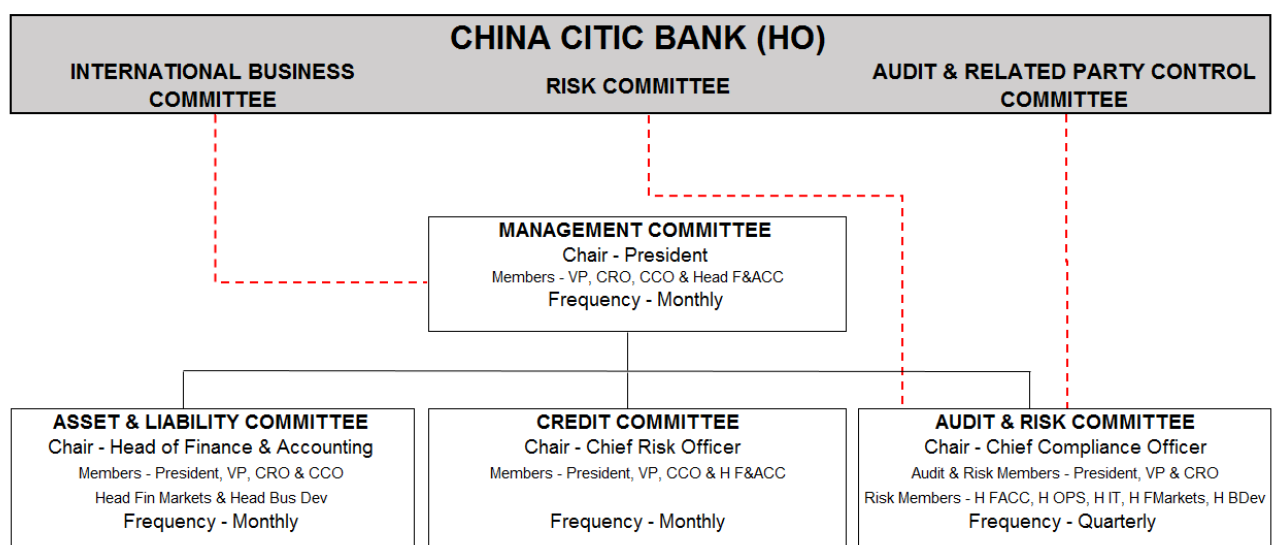


## 5 Risk Management Framework

The Risk Management Framework (“RMF”) seeks to ensure that there is an effective process in place to manage risk across the Branch.

Risk management is integral to all aspects of the Branches activities and is the responsibility of all staff. Senior Managers and Heads of Departments have a particular responsibility to evaluate their risk environment, to put in place appropriate controls and to monitor the effectiveness of those controls. The risk management culture puts emphasis on careful analysis and management of risk in all business processes.

These risks are identified, assessed and managed at both an enterprise level (‘top-down’) and business level (‘bottom-up’). Through both internal management and functional reporting lines, the Branch reports appropriate risk metrics to HO on a monthly and quarterly basis. The Branch’s Management Committee (“Manco”), which is chaired by the President, has oversight of these processes. This Committee meets monthly and provides a report on its activities to the Branch Audit & Risk Committee (“ARCo”), which meets quarterly and is responsible for reviewing and challenging all reports prior to submission to the relevant HO committees.



In order to have effective oversight of the above, the Branch will operate a comprehensive and robust risk management framework which will identify and manage all risks to which the business is exposed. The risk management framework operated by the Branch will be similar to that implemented by HO and sets out the roles and responsibilities of senior management and the committees.

The risk culture at CNCBLB sets an overarching framework for behaviours within the branch by establishing – both implicitly and explicitly – expectations about what is acceptable. Remuneration and reward arrangements within the branch play a predominant role in setting and reinforcing its cultural norms. The Chief Risk Officer attends all Committee meetings and provides the President with risk related information across the Branch so that it may be applied in the remuneration framework and making remuneration decisions. The Chief Risk Officer also updates the President and Management Committee on the branches' performance against the Risk Appetite Statement ('RAS'), which describes and measures the amount and types of risk that CNCBLB is prepared to take in executing its strategy. The President uses these updates in applying the remuneration policy and considering the risk related adjustments made to the variable pay pool, to ensure that return, risk and remuneration are aligned

The RMF is based on the 'Three Line of Defence model'. This allows responsibility and accountability to reside with the relevant persons and/or department, with ultimate responsibility for the Branch's risk framework residing with HO.

## 6 Business Risk Appetite

This section sets out what business activities (products, services and customer segments) the branch is authorised to carry out both by HO and the UK regulatory authorities. This means that any activities not included within this section will not be carried out by the Branch.

### 6.1 Customer /Counterparty/Issuer on-boarding

Customer Due Diligence (“CDD”) and Know Your Customer (“KYC”) are fundamental to risk management and, especially, are key anti-money laundering and counter terrorist financing policy requirements. CDD and KYC encompass knowledge, understanding and information obtained on a customer throughout the lifecycle of the relationship, including transactions and use of CITIC products/services. The risk appetite is defined as follows:

- The Branch has a zero appetite for conducting certain types of business which is in breach of the Money Laundering, Terrorist Financing and Transfer of Funds (Information on the Payer) Regulations 2017 & MLR 2019 (“MLRs”) or, otherwise, attracts a heightened level of AML and terrorist financing risk.
- The branch shall not operate accounts for shell banks and unlicensed banks or have any relationship with such entities, and will not operate anonymous accounts.
- The branch will not provide correspondent banking services or services to remittance agents, money bureaux money transfer agents or payment service providers.
- Client relationships in the following industries will not, ordinarily, be considered unless there is a special justification for doing so that addresses the enhanced risks these industries present -
  - Arms, military & defence
  - Precious metals and stones
  - Unregulated charities
  - Virtual currencies
  - Gambling

Full details and process are provided in the AML Policy and the ‘Onboarding Procedures for Customer and Counterparts’ held in Compliance Department.

## 6.2 Business Activities

CNCBLB will not conduct any retail business, but will undertake wholesale and commercial banking activities. The wholesale and commercial banking activities will be limited to the following:

Business Activity	Products
Financial Markets	<ul style="list-style-type: none"> <li>• Money Market instruments</li> <li>• FX Spot / Forwards / Swaps</li> <li>• Interest Rate Swaps</li> <li>• Liquid Bonds (UK Gilts/ US Treasuries or equivalent)</li> <li>• Corporate / FI Bonds</li> <li>• </li> </ul>
Banking	<ul style="list-style-type: none"> <li>• Transaction accounts (demand/call accounts)</li> <li>• Term Deposit accounts</li> <li>• Payment Services (Domestic and International)</li> <li>• Corporate Lending (Bi-lateral, club, syndication,...etc.) <ul style="list-style-type: none"> <li>• Domestic Guaranteed loan</li> <li>• General Purpose loan</li> <li>• Real estate loan</li> <li>• Revolving Credit Facilities</li> <li>• Project Finance</li> <li>• Asset-backed Finance</li> <li>• M&amp;A Finance</li> <li>• Leveraged Finance</li> </ul> </li> <li>• Loan origination, underwriting and syndication</li> <li>• Bond origination, underwriting and issuance</li> <li>• Trade Finance <ul style="list-style-type: none"> <li>• Bill and Telegraph Transfer financing</li> <li>• Letters of Credit (issuance, negotiation or risk participation)</li> <li>• Letters of Guarantees</li> <li>• Receivable financing</li> </ul> </li> </ul>

No business activity which would be caught within the scope of MiFID / MiFID II will be conducted without the sign-off from the President and Chief Compliance Officer.

All new products that may require additional regulatory reporting requirements, will be subject to the 'New Product Approval Process'. This process will require a detailed action plan to be implemented covering the launch of new products, including appropriate systems & controls to ensure compliance with all regulations.

### 6.3 Target Customers

The Branch will only transact with wholesale customers. The Branch's customer base can be split into four broad categories and these are listed below:

- **CITIC Group entities**

China CITIC Bank is a core part of the CITIC Group and has a natural advantage in acquiring business from within the Group or from customers of other Group Companies.

Products and Services	Example Group Customer	Access to customers
Corporate lending; loan origination, underwriting and syndication; daily payments and receipts of funds; FX risk management service	CITIC Construction, CITIC Heavy Industries, CITIC Dicastal, CITIC Pacific, CITIC Financial Leasing, CITIC Capital, and CITIC Securities	Through CITIC Group internal communication and coordination; and Group requirements.

- **HO Financial Institutions (Banks)**

CNCB currently has a network of more than 1,900 correspondent banks worldwide. CNCBLB will benefit from the same credit rating as CNCB (currently Moody Long-Term Rating Baa1 / Fitch Long-term Issuer Default Rating BBB) in the overseas market to raise funds from interbank market.

Products and Services	Potential Customer	Access to Customers
<p>Money Market and fixed income operation including interbank lending, issuing or purchasing CDs, Bond trading, credit asset transfer.</p> <p>Corporate lending, loan origination and syndication and trade finance services such as refinance, L/Cs and L/Gs.</p>	<p><b>UK FI customers:</b></p> <p>International banks and Chinese London based banks</p> <p><b>China FI customers:</b> China CITIC Bank branches, Chinese Banks branches &amp; subsidiaries outside China, Zheshang Bank, Guangdong Development Bank and other banks set up in Tier 2 or 3 cities in China.</p>	<p>Through the head office referral; customers' visits and road shows.</p>

- **HO Corporate and non-bank financial institutions**

Large-scale multinational enterprises operating in the EMEA region, including Chinese-funded enterprises always have strong financing capability, while their credit risk is relatively low and business income is relatively stable.

Products and Services	Potential Customer	Access to Customers
<p>Corporate lending, loan origination and syndication, FX and other risk management service.</p>	<p>BMW, Mercedes-Benz, Sino Pec, Sino Chem, China Oil, China Minmetals, China Investment Corporation, China Insurance Company, ANTA Sports, BAIC, KTK that have established long term solid relationships with CNCB HO.</p>	<p>China CITIC Bank London Branch will use China CITIC Bank's head office to get access to the potential customers</p>

- EMEA/Other Country Customers**

London Branch will build relationships with EMEA financial institutions and non-financial institutions, which have strong financing capability and low credit risk that provides stable business income for the Bank.

Products and Services	Potential Customer	Access to Customers
<p>Money Market and fixed income operation including interbank lending, issuing or purchasing CDs, Bond trading, credit asset transfer.</p> <p>Corporate lending, loan origination, underwriting and syndication, Trade Finance and international payments</p>	<p>Customers identified through Business Development Department's 2021/2 strategy and customer acquisition plan.</p> <p>Also includes Chinese Banks branches &amp; subsidiaries outside China that are not part of the existing HO financial institutions network.</p>	New customers to the Bank

### Customer / Product Matrix

The initial phase of CNCBLB customer services will have the following customer and product matrix:

Products		Customers			
Category	Product and services	<i><b>CITIC Group entities</b></i>	<i><b>HO Financial Institutions</b></i>	<i><b>HO Corporates &amp; Non-bank FI</b></i>	<i><b>EMEA Corporate/FI</b></i>
<b>Treasury</b>	Foreign Exchange (Spot Only)	√	√	√	√
	Foreign Exchange Forwards/Swaps		√		
	Interest rate / Cross-Currency Swaps		√		

	Interbank lending / borrowing		√		
	CD's		√		
	Repo's		√		
	Corporate Bonds		√	√	√
	High Quality Liquid Assets ("HQLA")		√		
<b>Corporate Loans</b>	Domestic Gtee loans	√		√	√
	General Purpose Loans	√	√	√	√
	Revolving Credit Facility	√		√	√
	Project Finance	√		√	√
	Asset-backed Finance	√		√	√
	M&A Finance	√		√	√
	Leverage Finance	√		√	√
	Loan / Bond origination/underwriting	√	√	√	√
<b>Trade Finance</b>	Financial Institutions (Refinance, SBLC's, Letters of Credit and guarantees)		√		
	Corporates (Bill advancing, Letters of Credit, guarantees, forfaiting and receivable finance)	√		√	√
<b>Deposit Products</b>	Corporate Current accounts	√		√	√
	Corporate Deposit Accounts	√		√	√
<b>Payment Services</b>	UK Domestic payments	√		√	√
	International payments	√		√	√



CNCBLB will not transact with Small Medium Enterprises (“SME”) and the Branch is aware that within the definition of Retail Customers the following criteria is used to classify SME business:

- Turnover is not more than £10.2 million per annum;
- Balance sheet total of not more than £5.1 million; and/or
- Number of employees is not more than 50.

There will be no customers classified as Retail (as per COBS 3.4).

## 7 Credit Risk

### 7.1 Credit Risk Exposure

Credit risk is the risk of loss due to one or more counterparties/borrowers/issuers defaulting on, or otherwise being unable to fulfil, their contractual obligations. Credit exposure will be generated by the following products:

Business Activity	Products	Country Risk	Obligor Risk	CP Risk	Issuer Risk	Pre-Settlement	Settlement Risk
Treasury	• Money Market instruments	√		√			√
	• Repurchase Agreements	√		√		√	√
	• FX spot	√		√			√
	• FX Forwards / Swaps	√		√		√	√
	• Interest Rate Swaps	√		√		√	√
	• HQLA / FI / Non-FI Bonds	√			√		
	• Corporate Bonds	√			√		
Banking	• Payment Services	√	√				√
	• Domestic Gtee loans	√	√				
	• General Purpose Loans	√	√				
	• RCF, Project Finance, Asset backed, M&A,						

	Leveraged Finance	√	√				
	• Loan origination/ underwriting and syndication	√	√			√	
	• Bond origination/ underwriting and issuance	√	√		√	√	
	• Bill and Telegraph Transfer financing	√	√				
	• Letters of Credit / SBLC's	√	√				
	• Letters of Guarantees	√	√				
	• Forfeiting/Receivable financing	√	√				

### **Definitions**

CNCBLB defines credit risk management in 5 categories:

1. **Country Risk** - risk that a foreign government will default on its financial commitments or restrict business/trade flows or the degree to which political and/or economic unrest impacts doing business in a particular country;
2. **Obligor Risk (Loans)** - also known as a debtor, potential default by entity who is legally or contractually obliged to make all principal repayments and interest payments on outstanding debt;
3. **Counterparty Risk (Money market/ financial instruments)** - the risk to each party of a contract that the counterparty will not meet its contractual obligations;
4. **Issuer Risk (Bonds)** – the legal entity that issues a financial instrument, any investor in the financial instrument incurs not only the market risk associated with any type of investment, but also an issuer-related default risk.
5. **Pre-settlement risk** – the risk that a counterparty defaults prior to maturity of a transaction which results in a market-to-market (plus credit add-on) exposure or replacement cost; this risk

is also present if CNCBLB act as agent/underwriter when issuing corporate loans and bonds (risk that the loan or bonds cannot be sold down); and

6. **Settlement Risk** – unless settled 'Delivery verse Payment' ("DVP") through an approved clearing house/exchange; settlement risk is the risk that a counterparty or intermediary agent fails to deliver cash or a security as per the agreement.

## 7.2 Credit Risk Mitigation

The following mitigants are employed by the Branch to help manage its exposure to credit risk:

- Avoiding concentrations of risk by limiting exposures to individual counterparties/borrowers and groups, and diversifying exposure across different counterparties, thereby reducing the impact of a single counterparty default;
- Ensuring robust initial and ongoing credit analysis of counterparties, groups and countries;
- Settlement of transactions through approved payment systems or on a delivery-versus-payment basis;
- Limiting exposures to individual countries and industry sectors, and diversifying exposure across different countries and sectors to the extent that it is possible within the constraints of the overall business model of the Branch;
- Setting limits on tenures of transactions with counterparties;
- Utilising netting and collateral agreements where possible;
- Ensuring robust documentation of transactions, including setting appropriate covenants, where possible; and
- Where possible, obtaining HO or third-party guarantees to reduce the risk of loss.

### 7.3 Credit Risk Appetite

The Branch has set its Risk Appetite in respect of credit risk as follows:

- No single obligor/counterparty/issuer should exceed 12.5% of the total credit exposure based on the Total Risk Weighted Assets ("TRWA") calculation.  
$$(EAD \times PD \times LGD / TRWA);$$
- Any related Group of obligors/counterparties/issuers should not exceed 25% of the total credit exposure based on the Total Risk Weighted Assets ("TRWA") calculation  
$$((EAD \times PD \times LGD + EAD \times PD \times LGD + EAD \times PD \times LGD + \dots) / TRWA);$$
- Provision coverage ratio of NPL  $\geq 150\%$ ;
- Non-Performing Loan ratio  $\leq 2\%$ ;
- Loan Book Portfolio - Average 12 months Default Probability of Corporate Business  $\leq 1\%$ ; and
- Treasury Portfolio - Average 12 months Default Probability of Financial Institutions Business  $\leq 1\%$

Furthermore, under the HO DOA provided to the President (see **Appendix A**), the Branch exposures must conform to the delegated authority agreed in the HO DOA.

The HO DOA will be reviewed at least annually and any changes to the approval will be incorporated into the RAS and communicated to the relevant members of staff. Further to the HO DOA, the branch implements additional credit control methodology to manage this risk, these measures include:

**Credit Risk Maturity Profile**

The following provides guidance for the risk appetite with respect to maturity of deals/transactions for Branch credit risk:

Business Activity	Products	Maximum Tenor
Treasury	<ul style="list-style-type: none"> <li>• Money Market instruments</li> <li>• Repurchase Agreements</li> <li>• FX Forwards / Swaps</li> <li>• Interest Rate Swaps</li> <li>• Liquid Bonds (Gilts/Treasuries or Equivalent)</li> <li>• Corporate Bonds</li> </ul>	1 year 1 year 5 years 5 years 10 years 5 years
Banking	<ul style="list-style-type: none"> <li>• Domestic Gtee'd loans</li> <li>• General Purpose Loans</li> <li>• Real Estate Loans</li> <li>• Revolving Credit Facilities</li> <li>• Project Finance &amp; asset backed finance</li> <li>• M&amp;A and Leverage finance</li> <li>• Bill and Telegraph Transfer financing</li> <li>• Letters of Credit</li> <li>• Letters of Guarantees</li> <li>• Forfeiting/Receivable financing</li> </ul>	5 years 5 years 5 years 5 years 5 years 5 years  2 years 2 years 2 years 1 year

**Credit Risk mitigation (acceptable collateral)**

Collateral Type	% Haircut/Loan to Value	
	Financial Institutions	Corporate
Cash	100%	100%
Bonds	Custodian/Clearing haircuts – credit quality, maturity/currency	Depending on assessed credit quality & liquidity
Tradeable Equities	N/A	50%

<b>Receivables</b>	N/A	33% of debtors book excluding +180 days
<b>Credit Derivatives/Other direct credit substitution</b>	100%	100%
<b>Bank guarantees/Letters of Credit</b>	Depending on assessed credit quality	Depending on assessed credit quality
<b>Asset Backed</b>		
- Residential Real Estate	N/A	70%
- Commercial Real Estate	N/A	60%
- Industrial Real Estate	N/A	50%
<b>Structured Real Estate projects &amp; Other assets</b>	To be determined by CCO	To be determined by CCO

### **Credit Concentration Risk**

Concentrations can arise with regard to material individual exposures to a single counterparty or group of connected counterparties, to exposures to counterparties located within a particular geopolitical region, or exposures to counterparties from a particular industrial sector. Any such concentrations could leave the Branch vulnerable to a stress that could potentially impact CNCBLB meeting its strategic objectives.

Therefore, the Branch has set Risk Appetite limits in relation to these concentrations as detailed below: Credit Risk Concentration Matrix

Risk category	Risk type	Risk measurement	Risk appetite Maximum Exposure		
<b>Risk Profile</b>	<b>Total RWA</b>	<b>HO Internal Rating</b>	CR	Rate	%
			1	AAA+	100
			2	AAA	100
			3	AA+	90
			4	AA	80
			5	A+	70
			6	A	60
			7	BBB+	50
			8	BBB	40
			9	BB+	30
			10 below	BB B	20 10
<b>Geography</b>	Country risk exposure	Net exposure to Total Assets: China United Kingdom United States of America Europe (excluding UK) Total Other Countries (Maximum 20% per country)			100% 100% 100% 80% 50%
<b>Sector</b>	Industry and sector exposure	Net exposure to Total Assets: Financial – Banks Financial – Other Services Real Estate Construction/Infrastructure Manufacturing Retail/Wholesale trade Business services & TMT Energy, utilities & health care Sovereign/Government Mining & Natural resources Total Other Industries			80% 50% 50% 35% 30% 25% 25% 25% 20% 20% 20%

Credit Monitoring (for guidance only)			
<b>Currencies</b>	Approved currencies	Net exposure to Total Assets: USD RMB GBP EURO Total Other Currencies (Maximum 25%)	100% 100% 50% 50% 50%
<b>Customer Type</b>	Exposures to customer types	Net exposure to Total Assets: Sovereign/Government Financial Institutions Corporate	50% 60% 75%

Customer/Product matrix	Product Concentration Limits as a maximum % of Loan Book		
	Loans Domestic gtee/General purpose/ Basic RE	Loans Project / structured /Leveraged	Trade Finance SBLC/LC/LG/Structured
CITIC Group Entities	50%	50%	50%
HO FI	60%	60%	60%
HO Corporate	75%	50%	50%
EMEA /Other Country Customers	50%	50%	50%

The management of credit risk, including the above risk appetites and concentration limits, are defined in detail in the '***Credit Approval and Credit Risk Policy***'.

## 8 Market Risk

### 8.1 Market Risk Exposure

Market risk is the exposure to adverse changes in the market value of financial instruments caused by market factors such as changes in interest rates, foreign exchange rates and volatility. Foreign exchange risk and interest rate risk are the primary forms of market risk which the Branch is exposed to through lending in currencies other than base currency, lending at fixed rates and treasury operations.

Financial Markets department are responsible for managing market risk which is detailed in the HO Financial Markets delegated authority, as defined under the HO Branch DOA, with specifies product approvals, stop-loss limits and trading limits across the three main financial market operations:

- Trading Business (FX and Interest rate)
- Foreign Currency Bond Investments (Government, FI, Corporate & hedging instruments)
- Foreign Currency Treasury Business (Internal & Interbank borrowing/lending, Repos and non-trading derivatives)

See **Appendix B** for details on product approval and limits.



The ManCo and the ALCo both have responsibility for monitoring the market risk and have set internal guidelines for CNCB LB Financial Markets, these comprises mainly of:

## 8.2 Foreign Exchange Risk

Foreign exchange risk refers to the risk of on and off-balance sheet businesses of a bank incurring losses due to unfavourable changes of exchange rates. The Branch will measure foreign exchange risk mainly through the analysis of foreign exchange exposures that consist of trading and non-trading exposures, including trading exposure that mainly results from the position in foreign exchange trading and non-trading exposure that mainly arises from foreign currency capital and foreign currency profit. The calculation of a Foreign Exchange ("FX") Net Present Value/Delta ("NPV") for its FX risk exposure for all currencies. FX NPV is calculated by estimating the present value of each position by using the forward curve implied interest of each currency

Proprietary trading	Description
Currencies	G7 currencies plus CNY, SGD and HKD  G7 currencies include USD, EUR, GBP, JPY,AUD, NZD, CAD and CHF
Overnight Net Open Position limit	\$2 million

## 8.3 Interest Rate Risk

Interest rate risk refers to the risk of losses to overall earnings and economic value of bank accounts resulting from unfavourable changes in factors such as interest rate and maturity structure, including re-pricing risk, yield curve risk, benchmark risk and option risk.

CNCBLB's tolerance for interest rate risk remains relatively high in the current market of flat interest rate curves and forecast economic outlook. Interest rate risk is created due to borrowing funds with short dated maturities and lending them over a longer term but CNCB's funding has changed over the last 6 months and is now more diversified between HO (evergreen and commercial funding) and short/medium term Certificates of Deposits and longer term CNCB bond issuance.

CNCBLB manage interest rate risk using a 'gap' approach for measuring Interest Rate Risk in the Banking Book, ("IRRBB") exposure. This is determined as the maximum net position of interest earning assets and interest paying liabilities utilising actual maturity or maturity for interest rollover whichever is earlier.

Gapping Limits - Interest rate gapping limits are set in order to control CNCBLB's exposure to the interest rate risk arising from its business activity and restricts the re-pricing risk over various maturity buckets. The degree to which CNCBLB would be exposed to interest rate risk is identified through gap analysis using the principle of grouping together assets and liabilities that are affected by interest rate changes according to their maturity dates. Two different types of gaps may occur:

- A **negative gap** occurs when interest-sensitive liabilities maturing at a certain time are greater than interest-sensitive assets maturing at the same time. This results in a net exposure if interest rates rise by the time of maturity;
- A **positive gap** occurs if the amount of interest-sensitive assets maturing in a certain period exceeds the amount of interest-sensitive liabilities maturing at the same time. In this situation the firm will be negatively impacted if interest rates fall by maturity.

It is evident from the current business model that CNCBLB's interest rate risk in the Loan Book is carefully managed with most loans reflecting short-term floating interest rates (EG: 1/3/6 months Libor) which can be match funded in the market. Long dated fixed interest rate risk remains unhedged but Treasury are working on hedging products such as interest rate swaps whereby CNCBLB can lock in the margin and remove any interest rate risk over the life of the contract or partially, due to restricted credit limits.

In the current market with flat interest rate curves, the risk appetite for interest rate gapping is articulated in the following table:

Estimated Balance Sheet size for 2021 is USD 2,000,000,000

Tenors	Gapping Exposure USD millions (Positive or Negative gaps)
Up to 1 month	1,000
Up to 3 months	1,000
Up to 6 months	900
Up to 12 months	800
Greater than 12 months	700

The Branch will manage its interest rate risk for the overall objective of observing the principle of prudent risk preference and achieving steady growth of both net interest income and economic value within the acceptable range of interest rate risk. The management of market risk, including the above risk appetites and concentration limits, are defined in detail in the '**Market Risk Policy**'.

## 9 Operational Risk

### 9.1 Operational Risk measurement

Operational risk is the risk of an economic loss, a disruption to business, an adverse impact on reputation or on client relationships or of legal action arising from inadequate or failed internal processes, people and systems. Operational risk will generally occur due to either inadequate or failed internal processes, staff, IT systems or other external factors. Within this broad classification, the Branch will identify a number of categories of operational risk that are aligned with market standards under the regulatory requirements:

OPERATIONAL RISK	BASEL EVENT TYPE	DESCRIPTION
PEOPLE RISK	Internal Fraud	Losses due to acts of a type intended to defraud, misappropriate property or circumvent regulations, the law or company policy, excluding diversity/ discrimination events, which involves at least one internal party
	External fraud	Losses due to acts of a type intended to defraud, misappropriate property or circumvent the law, by a third party
	Employment Practices and Workplace Safety	Losses arising from acts inconsistent with employment, health or safety laws or agreements, from payment of personal injury claims, or from diversity/ discrimination events
PROCESSESS RISK	Clients, Products & Business Practices	Losses arising from an unintentional or negligent failure to meet a professional obligation to specific clients (including fiduciary and suitability requirements), or from the nature or design of a product
	Execution, Delivery & Process Management	Losses from failed transaction processing or process management, from relations with trade counterparties and vendors
	Business disruption and system failures	Losses arising from disruption of business or system failures
SYSTEMS RISK		
EXTERNAL RISK	Damage to Physical Assets	Losses arising from loss or damage to physical assets from natural disaster or other events

The operational risk management of the Bank follows the principle of “comprehensive management, clear responsibility, tiered control, and fulfilled responsibility”. As for the operational risk management, the Bank implements identification, assessment, monitoring, control, mitigation and reporting of operational risk through the establishment and improvement of the operational risk management framework. Besides, the Bank takes effective control measures to reduce the loss of operational risk, promote the construction of operational risk management system and constantly improve the operational risk management mechanism of dynamic management and continuous improvement.

The four operational risk tools that will be used to identify, measure, manage and report operational risk are:

- Incident/Near miss log (includes root cause analysis, corrective and preventative actions)
- Risk & Control Self-Assessments (Departmental risk identifications and controls)
- Key Risk Indicators (monitoring and reporting of key risks to senior management)
- Scenario analysis (conduct and non-conduct risk scenarios that could negatively impact CNCBLB)

## **9.2 Operational Risk Appetite**

The Risk Appetite with respect to operational risk is as follows:

CNCBLB is a start-up operation and therefore has no historical data and may be subjected to higher people, processes and system risks in the initial stage of its strategic development. In order to quantify an acceptable risk appetite for operational risk exposure, a dynamic methodology will be

monitored by risk department to manage the higher risk in the initial stages; this risk will reduce as the people, process and systems are strengthen over time, the following table refers:

	Year 1	Year 2	Year 3	Year 4	Year 5
<b>Operating Income</b>	\$3,100,000	\$5,600,000	\$11,100,000	\$17,300,000	\$23,600,000
<b>Tolerance Risk Appetite (bps)</b>	1.25	0.85	0.50	0.25	0.25
<b>Ops Risk Appetite</b>	<b>\$38,750</b>	<b>\$47,600</b>	<b>\$55,500</b>	<b>\$43,250</b>	<b>\$59,000</b>

The management of Operational risk, including the above risk appetites and concentration limits, are defined in detail in the '**Operational Risk Policy**'.

## 10 Liquidity Risk

### 10.1 Liquidity Risk exposure

Liquidity risk is the risk that the Branch does not have sufficient liquidity resources available to enable to it meets its payment obligations as they fall due. Liquidity risk can also take form if the Branch is unable to obtain adequate funding in a timely manner at a reasonable cost.

Liquidity risk management will be managed by HO on a Group-wide basis, the Branch is expected by HO to develop and maintain appropriate liquidity policies and limits to ensure it to operate prudently on a day to day basis. The Branch will operate an Asset and Liability Committee ("ALCo") which will be supported by ManCo in ensuring ongoing adherence to the limits set for liquidity risk.

The Branch management will monitor its liquidity risk appetite through the ALCO meetings and within an approved 'Liquidity and Funding strategy' that will provide guidance to Financial Markets on the expected balance sheet structure.

This optimal balance sheet structure will depend on the product approvals covering longer term funding products, these could include:

- CD's (Certificate of Deposit program out to 365 days)
- Medium/Long term bond issuance
- High Quality Liquid Assets (REPO facilities to raise funds)
- Customer deposits

Short term (under 30 days) liquidity risk is managed using 'Whole-Bank' liquidity management and monitored and reported through the Group Liquidity Coverage Ratio ("LCR"). The branch management will monitor liquidity risk through the ALCO approved 'Liquidity and Funding strategy' and the '*Liquidity Risk Policy*'.

## **11 Other Risks**

### **11.1 Legal Risk**

Legal risk is the risk of loss caused by a transaction failing to perform in the way expected due to failure to correctly document, enforce or adhere to contractual arrangements, or due to the legal process failing to enforce the terms of a contractual arrangement or due to a change in the law.

Note that the risks associated with legal actions arising from the Branch's activities are considered to be operational risks associated with those activities. The Branch identifies two key sources of legal risk in its business:

- **Lack of documentation or legally ineffective documentation:** transacting with counterparties prior to completing documentation or executing on the basis of ineffective documentation; and
- **Reliance on enforcement of netting and collateral agreements or guarantees:** evaluating credit exposures on the assumption that: (a) netting arrangements within the trade documentation; and/or (b) collateral agreements and/or (c) guarantees will be enforceable, or will apply, in the event of a counterparty default.

The Branch has zero appetite for legal risk and must ensure the highest level of legal protection from appropriate legal advisors prior to any transaction being executed and if required, any changes that may occur during the life-span of a transaction.

The risk management process implemented will ensure a high level of due diligence in the identification, monitoring, reporting and management of Legal risk to ensure that the Branch understands that legal risk can crystallise from time to time and actions plans are in place to deal promptly and decisively with any such situation.

## 11.2 Compliance and Regulatory Risk

The Branch defines compliance and regulatory risk as the failure to meet UK and/or Chinese regulatory requirements and the potential impact of changes in regulatory rules. In terms of compliance risk, the risk is caused by failing to adhere to policies, procedures and framework as mandated by Head Office, the UK regulations or internal policies and procedures. The Branch is aware that as part of its day to day operations it will open itself to many different forms of compliance risk such as transaction reporting, treating customers fairly, best execution, bribery & corruption rules, anti-money laundering (“AML”), financial crime and conduct risk.



From a conduct perspective, The Bank will only offer its customers “plain vanilla” services and products, and will ensure that its staff training and documented processes and procedures, are of sufficient standard to minimise the risk of compliance failures or reputational issues arising from its dealings with customers.

The Branch accords the highest importance to complying with applicable internal processes, policies and banking regulation at all times and has no appetite for any breach of policies, laws, regulatory rules or requirements.

### **11.3 Climate Change Risk**

Environmental risk and the connectivity to other risks remains a risk factor that CBCNBLB risk department will monitor across its loan book and financial assets. The change in climate through natural disasters, human-made environmental disasters, extreme weather events and potential failure of any mitigation could impact various other existing and emerging risks.

CNCBLB management considers climate change risk in two categories, these risks are defined as:

1. **Physical risks from Climate change:** climate change risk from a physical aspect includes the global increase of more frequent or severe weather events like flooding, droughts and storms. These events bring ‘physical risks’ that could impact society directly and have the potential to have severe impacts on underlying economies.

The risk that these events occur more frequently, society will become more reliant on insurance to cover the costs of damage to assets. If companies and households are not insured against these events then the cost of the loss of the assets could be substantial and have considerable impact on asset prices and the overall economy.

2. **Transition risks:** this climate change risk materialises when a decision is made to move towards a less polluting and greener economy. In any transition, risks evolve that could impact some sectors of the economy that could face big shifts in asset values or higher costs of doing business. The speed of transition to a greener economy is a significant risk factor that could severely impact certain industries and potentially damage the financial stability of the economy.

The shift towards a greener economy could have substantial impact on the value of investments held by banks and insurance companies in sectors like coal, oil and gas, motor, ships and planes, or other industries that use a considerable amount of energy to make raw materials like steel and cement.

CNCBLB have identified this as a risk, within the Risk Appetite statement and management will consider 'Climate Change Risk' in all business going forward. This will be essentially considered under the Industry analysis in all credit applications, where Risk Department will provide an analysis of financial risk due to climate change. The CRO will continue to work with CNCB Head Office with regards to desirable and non-desirable industries that could impact the Bank's sustainability and profitability.

#### 11.4 Strategic Risk

Strategic risk is the risk of an external or internal event preventing the Branch from achieving its objectives. The Branch has identified the following sources of strategic risk to its business:

- **Economic risks:** changes in interest rates, global growth and other macroeconomic risk factors;

- **Competition:** competition from other Chinese Banks based in the UK or Europe, and from other Chinese financial institutions looking to develop their presence in Europe;
- **Significant Losses:** significant losses, particularly from credit events, but also from market movements, or regulatory action could severely impact the Branch's ability to achieve its objectives;
- **Political and Regulatory Risk:** for instance consequences of Brexit or a change in the regulatory approach to non-EEA branches in the UK; and
- **Staffing:** The Branch has a limited number of staff to carry out its business and it is a critical risk to attract and retain the right staff to meet the strategic objectives.

The Branch has the following mitigants in place:

- Discussion of emerging issues in all committees;
- Staff meeting discussions;
- Periodic video conferencing with HO;
- Network meetings with related parties;
- Policy guidelines;
- Regulatory inputs;
- Interactions with external skilled persons/consultants; and
- Internal/external audit reports.

### 11.5 Conduct Risk

Conduct risk is managed in both Compliance and Risk Departments, as this risk relates to the internal risk culture, customers being treated unfairly or being disadvantaged by the actions of the Branch. The Branch has adopted local policies as a framework for conduct risk that reflects the UK regulatory environment. It also includes the risk of failing to meet market rules or standards, or

general laws covering the Branch's activities. Any breach of the conduct rules will reportable to ManCo and the UK regulatory authorities.

The Branch has no tolerance for any breaches of conduct rules, code of conduct and market standards. CNCBLB acknowledges that conduct risk could occur at a number of points on the customer journey, from the design of the product, to the way the product is sold, to the ongoing servicing of clients' needs. The senior management of the Branch recognise that governance and the underlying culture of the organisation will be central to the management of conduct risk.

The Branch will operate in the wholesale market and not in the retail market space, and its clients will be categorised as MiFID Eligible Counterparty or Professional. The Branch will thus develop its conduct risk framework to appropriately identify, monitor and manage the universe of pertinent potential wholesale conduct risks.

At a high-level conduct risk can be divided into five categories:

- **Failure to consider our client's needs:** Can include the selling of inappropriate products to clients or inadequate ongoing review of products and services for clients;
- **Failure to treat clients fairly or to act in their best interests:** Can include providing misleading marketing information on products, pricing products inappropriately, failing to provide best execution of client orders, failing to deal appropriately with client complaints;
- **Failure to meet required standards:** Intentionally or unintentionally failing to meet market rules or standards, or the general regulatory or legal framework within which business is done, including anti-bribery and corruption legislation or sanctions rules;
- **Failure to implement systems infrastructure adequate to meet clients' needs:** Where for example, operations and systems are set up in such a way that the ability on the Branch to

transact business in a reliable and transparent manner is hampered by poor systems infrastructure and/or maintenance; and

- **Failure to implement governance arrangements or management information to enable effective oversight or management of conduct risk:** The Branch may inadvertently increase the incidence of conduct risk by not taking appropriate steps to organise and maintain the oversight of conduct risks within its business.

To support the management of conduct risk, CNCBLB will determine and monitor a set of Key Risk Indicators (“KRIs”). The Chief Risk Officer will be responsible for the establishment, maintenance and the monitoring of these KRIs and on a monthly basis providing Management Information (“MI”) to the ManCo. If certain KRI trigger thresholds are breached, this will be reported with a recommendation for mitigating action and a target remediation date to the Chief Compliance Officer, the ARCo and the ManCo.

### 11.6 Outsourcing Risk

The Branch considers outsourcing risk a sub-set of operational risk management framework and defines this risk as the failure to have effective oversight of existing and proposed outsourcing arrangements. All outsourcing and third-party arrangements will be in-line with FCA SYSC 8 and take reasonable steps to avoid undue additional operational risks, this will include assurance that outsourced function do not impair:

- The quality of internal controls; and
- The ability for the regulators to monitor the Branches compliance with all obligations under the regulatory systems relevant to the Branch.

CNCBLB is aware that in undertaking outsourcing activities, the process gives rise to several risks that need to be appropriately mitigated:

- **Business Strategy Risk** – the risk arising from erroneous business decisions, improper implementation of decisions or lack of responsiveness to industry changes. This risk is a function of the compatibility of organisation's strategic goals, the business strategies developed to achieve those goals, the resources deployed against these goals and the quality of implementation. The service provider may conduct business on its own behalf, which is inconsistent with overall strategic goals of the Branch;
- **Reputational Risk** – the risk arising from negative public opinion. The risk may expose the institution to litigation, financial loss or a decline in customer base. Poor service from the service provider and its customer interaction not being consistent with the overall standards of the Branch;
- **Legal and Compliance Risk** – The failure of a service provider in observing with UK legal and regulatory requirements can lead to levying of fines, penalties or punitive damages, resulting from supervisory actions. Additionally, risks arise from the degree of certainty the Branch has in respect of enforcing a contract;
- **Operational Risk** – This risk arises due to technology failure, fraud, error, inadequate financial capacity to fulfil obligation and/or provide remedies;
- **Exit Strategy Risk** – This could arise from over-reliance on one firm, the loss of relevant skills in the Branch itself preventing it from bringing the activity back in-house and contracts entered into wherein speedy exits would be prohibitively expensive; and
- **Concentration and Systemic Risk** – Due to lack of control of the Branch over a service provider, more so often when overall banking industry has considerable exposure to one service provider. Failure of a service provider in providing a specified service, a breach in

security/confidentiality, or non-compliance with legal and regulatory requirements, among others may lead to reputation / financial losses for the Branch and may also result in systemic risks within the banking system in the country.

The Chief Risk Officer will be responsible for the adequacy of the outsourcing risk framework implemented by the Branch as detailed in the Outsourcing Policy. Within this framework, individual SMFs will be allocated responsibility for the relationship with specific service providers.

On engaging with a service provider, the business owner and risk department undertakes a risk assessment exercise in conjunction with the prospective service provider. This assessment is used to identify the key risks associated with the proposed service(s) to be outsourced. The business owner is also required to develop, in partnership with the service provider, a methodology covering system and controls to manage the risks identified. The details of the risk assessment and the KPIs used for managing this risk is covered in the Branch's Outsourcing Policy.

## **12 IT Risk**

The Branch defines IT risk as the failure of computer and infrastructure related to IT. It is the risk of a threat exploiting vulnerability of an IT based asset or group of assets which will in turn cause harm to the organisation.

The Branch will have detailed IT risk management methods, to improve the security protection of the computer systems, networking and production environments. In addition, a comprehensive and effective IT risk management framework will be implemented and will adhere to the HO's "IT Risk Management Regulations".

### 13 Pandemic Risk

The branch defines a pandemic as a global outbreak of a disease. Pandemics happen when a new virus emerges to infect people and can spread between people sustainably as there is little to no pre-existing immunity against the new virus, it spreads worldwide.

Manco will always put staff health and safety first but will act in accordance to UK Government and/or World Health Organisation advice. In such events, the branch will invoke its 'Business Continuity Plan' which could include the following phases:

#### **Phase 1**

- Department shift work – Head of Departments to agree staff arrangement to split their departments into weekly office/home teams.
- Flexible hours – Head of Departments to agree with staff flexible hours to attempt to avoid London rush-hours.
- Head of HR to arrange daily monitoring of staff members health and ability to work

#### **Phase 2**

- All staff work from home - full work from home invocation due to lock-down of London

#### **Phase 3**

- Staff ill/unable to work – back-up plan to be put in place to cover all critical positions requiring 2 people authentication process
- Head of IT to ensure Head Office support/back-up available to change existing system control protocols in emergency situations.

#### **Phase 4**

- Return to work – guidance to be developed to determine when it is safe to return to work



## **14 Risk Appetite Statement - Governance**

The governance framework around the Branch's RAS along with roles and responsibilities are covered in the Risk Management Framework. The local responsibility for the review and challenge of the RAS lies with ManCo, within the criteria set in the DOA and oversight of HO's International Business Committee.

### **14.1 Exceptions**

Circumstances may arise whereby the business wishes to pursue an opportunity outside the Branch's agreed Risk Appetite (and by extension the President's delegated authority "DOA"). Unless otherwise provided for in this document, the opportunity must first be reviewed and approved by the ManCo and then escalated to HO for final approval.

Only following approval by the ManCo and the HO can any such opportunity be pursued.

### **14.2 Stress Testing**

A stress testing framework will be developed by the Risk department to provide stress scenario analysis and testing on a periodic basis. This will be developed overtime using income statement and balance sheet data to determine both idiosyncratic and market stress scenarios and will be based on the Risk Appetite parameters defined in this document, regulatory business plan and risk policies.

Results of the scenario analysis and stress testing process will form the foundation of the stress-testing framework which will be presented to the ARCo and ManCo. This framework will provide the basis for the review of the RAS and will inform senior management of the appropriateness of the

Risk Appetite quantification and whether or not any amendments should be considered to the size of the Risk Appetite or associated limits.

### 14.3 Management Information and Reporting

Management Information ("MI") will be produced on a regular basis and these will contain metrics based on the stated appetites contained within the RAS. MI relating to the branch performance against its stated Risk Appetite measures will be included within the regular reporting received by the ManCo (monthly) and the ARCo (quarterly).

In addition, the Risk department will monitor the Risk Appetite limits daily and report at least weekly with monthly presentations of compliance at the ManCo and ARCO meetings. In the event of a breach of RAS, the specific circumstances must be reported in accordance with section 14.4 below.

### 14.4 Escalation of RAS Breaches

The Risk department through the CRO will be responsible for escalation of breaches to the respective committees. The escalation procedure differs depending on the nature of the breach:

- **Risk Appetite Metric:** Breach of the Risk Appetite parameters; and
- **Management Action Limits:** Breach of parameters set by ManCo (in order to provide early-warning triggers as key ratios approach the Risk Appetite threshold).

**Figure 1 RAS Escalation Points**

Report to	Timing	Responsibilities
<b>Risk Appetite</b>		
ManCo	Immediate	Review challenge and approve corrective actions, and oversee corrective action(s)
ARCo	Immediate	Oversee implementation of corrective action(s)
<b>Management Action Limit</b>		

ManCo	Regular MI pack	For information
ARCo	Immediate	Oversee implementation of corrective action(s)

While escalation of a breach would be immediate (aim for this to occur within the working day on which the breach was identified), the relevant authority in conjunction with the Risk department shall provide to ManCo a more detailed explanation along-with the steps being taken by the Branch within a period of three working days.

#### 14.5 RAS Usage in CNCBLB

The RAS is set out in sufficient detail to enable ManCo and ARCo to review and the risk profile of the Branch and report to HO Risk Committee. Compliance with this RAS is mandatory and will be monitored and reported in accordance with the risk management processes set out in the Risk Management Framework.

#### 14.6 RAS Approval and Update

The RAS has been prepared by the CRO and it will be reviewed, challenged and approved by the ARCo and ManCo at least annually or more frequently should changes in the business plan or activities occur.

**15 Appendix A – HO Branch Delegated Authority**

**16 Appendix B – HO Financial Markets Delegated Authority**